

Malaysian Experience in Financing Private Forest Plantation

Mohd Shahwahid Haji Othman

Deputy Dean, Faculty of Economics & Management,
UPM

Is there a need for forest plantation in Malaysia? Answer is Yes! Why

- i) Virgin production natural forest is running down even though the production permanent reserved forest land area is secured
 - Previous excessive forest openings for harvesting require correction & future annual harvesting coupe has to be reduced.
 - ii) Rubber tree stands have declined owing to reduced replantings in favor of oil palm planting and conversions to other land uses.
- =>Effects are a decline in domestic log production & the inability to meet domestic processing capacities

But why is investment in forest plantation lagging?

- Private sector investment in forest plantation is hampered by
 - the long gestation period
 - the high initial cost of production
 - high accumulated interest charges
- Scarcity of large contiguous land for forest plantation

Malaysian Government has to intervene in the interest of the wood-based industry through:

- **Formulating a Forest Plantation Development Program**
 - The recommended trees species for forest plantation development program are:
 - *Hevea brasiliensis* (Rubber)
 - *Acacia mangium* / *Acacia hybrid*
 - *Khaya ivorensis* (African Mahogany)
 - *Tectona grandis* (Teak)
 - *Azadirachta excelsa* (Sentang)
 - *Neolamarckia cadamba* (Kelempayan / Laran)
 - *Falcataria mollucana* (Batai)
 - *Octomeles sumatrana* (Binuang)
- **Establishing a special purpose vehicle (SPV) company to provide financial loans to interested private forest plantation venture**
 - Forest Plantation Development Sdn Bhd,

Strategic Provision of

- (i) financial assistance through soft loans and
- (ii) Other incentives (Investment Tax Allowance and Pioneer Status) along
technical support and training

Functions of the SPV company

- **To promote** the establishment of forest plantations for future sustainable timber supply.
- **To obtain** enough funds either locally or internationally to support the establishment of commercial forest plantations.
- **To provide** soft loans to state government agencies and private companies interested in development of forest plantations.
- **To standardize** all establishment activities and implementations of forest plantation silvicultural management on areas under the program.
- **To create** a proper trading centre for timbers produced by man-made forests.
- **To provide** advice on all aspects especially in updating the ministerial on issues pertaining to lands, investment opportunity, new policy and guidelines, and to initiate the new investment program.

Objectives

- **To further** encourage commercial forest plantations establishment.
- **To sustain** material supply for the timber industry.
- **To increase** investment in timber industry.

(i) Funding Forest Plantation Development Program

- Commercial Scale
- Small and Medium Scale
- Agroforestry

Commercial Scale

CRITERIA FOR FUNDING

- Eligible Application of soft loan to the SPV :
 - For non-public listed company: company should be Malaysian-owned with 100% local equity and registered under the Companies Act 1965;
 - For public listed company: company should have at least 51% local equity and registered in Malaysia under the same act.
- Minimum paid-up capital of at least RM500,000;

- Land: privately own or have at least 30 years leasehold agreement with minimum size of:
 - 2,500 ha for rubberwood and 15,000 ha for other recommended trees species for 15-year cycle (Peninsular Malaysia); and
 - 15,000 ha for rubberwood and other recommended trees species for 15-year cycle (Sabah and Sarawak)

Peninsular Malaysia:

- must be on state lands or alienated lands and not on Permanent Reserved Forests (PRFs).

Sarawak:

- Only areas with License for Planted Forest (LPF).

Sabah:

- Only areas approved as zone for Industrial Tree Plantation (ITP) under the Sustainable Forest Management License Agreement (SFMLA);

Commercial Scale: Criteria for Funding

- Company must have sufficient planting materials that are certified by the Malaysian Rubber Board (MRB) for rubber clones (latex timber clones) and Forest Research Institute of Malaysia (FRIM) for other trees species.
- Company must be able to finance 10% and 20% the cost of the proposed project for rubber and other trees species, respectively;
- Land for forest plantation must be free from other crops such as oil palm and cocoa and the fund is for the planting and maintenance of recommended trees species.
- Company should prove to be financially strong with satisfactory and reasonable cash-flow
- Companies should not have any adverse record of borrowing from any financial institutions or government agencies.

Commercial Scale

- ***LOAN APPLICATION***
- The documentations needed are:
- Application Letter
- Company Profile
- Working Paper of the Proposed Project
- Copies of Form 9, 24 and 49 under the Company Act (to be verified)
- A copy of Memorandum Article of Association (to be verified)
- A copy of Land Title [Ownership] (to be verified)
- Company's Organization Chart (Forest Plantation Management Division)
- ***WORKING PAPER FORMAT***
- Standard format of working paper of the proposed project for financing are as follows :
- Objective and Scope of the Project;
- Background of the Project;
- Project Location and Hectarage (Attach map of the project);
- Project Details including tree species to be planted;
- Prospect of the project;
- Implementation Plan (Planting Schedule);
- Project Costs (List all items and costs in detail);
- Project financing (Percentage of financing needed and company's own financing);
- Marketing proposal for the timber production (for own use or to be sold elsewhere);
- Project cash flow for 15-year period; and
- Company Financial Statement (to be verified).

Small and Medium Scale

CRITERIA FOR FUNDING

- The company must be Malaysian-owned with 100% local equity and registered under the Companies Act 1965 or Cooperative Act 2007;
- Company possesses a minimum paid-up capital of at least 10% from the value of loan applied.
- The applicant's land should either have a permanent title or have at least a minimum of 20 years leasehold (supported in writing from the state authority).
- The land size should range between 4 ha to 2,500 ha.
- The company is required to purchase sufficient planting materials from FPDSB and/or its authorized representatives.
- The company should prove to be financially strong with satisfactory and reasonable cash-flow.
- Companies should not have any adverse record of borrowing from any financial institutions or government agencies.

Grant Scheme for Agroforestry

CRITERIA

- The land is either an own land ownership with a permanent title or have at least a minimum of 20 years leasehold
- The suitable land should be < 4 ha.
- The applicant is required to purchase sufficient planting materials from FPDSB or authorized representative of FPDSB.

Financing Commercial Scale

SUCCESSFUL APPLICANTS WILL BE OFFERED THE LOAN WITH THE FOLLOWING TERMS AND CONDITIONS:

- Maximum loan for each borrower is 80% of project cost and for development of forest trees plantation only.
- Grace period for soft loan repayment is 15 years and the loan period is 20 years.
- Management fees of 3.0% compounded on yearly basis for the first 15 years and thereafter on daily basis i.e. from year 16 and onwards.
- Payback period soft loan plus management fee is 5 years and it begins on 16th year.
- Borrowers need to furnish quarterly report on the development of the plantation project in accordance with the Forest Management Plan.
- Tapping of LTC of rubber clones can commence during the 8th year. On tapping the borrowers can start repayment of loan by providing 30% of the net profit.

Small and Medium Scale Plantation Establishment

- ***SUCCESSFUL APPLICANTS WILL BE OFFERED THE LOAN WITH THE FOLLOWING TERMS AND CONDITIONS:***
- Management fee of 3.0% is compounded annually for 15 years (grace period) and will be compounded on daily basis during the payback period (5 years) that commences on year 16.
- Grace period for soft loan repayment is 15 years and the loan period is 20 years.
- The harvesting right of trees on the project land need to be assigned to the lender until the borrower has fully paid the loan facility. Prior consent from the lender is needed before taping or harvesting.
- Borrowers need to furnish quarterly report on the development of the plantation project in accordance with the Forest Management Plan. Failing which the facility can be terminated or penalty can be imposed on the borrower.
- No two companies with a common shareholder can apply this facility.
- The loan facility will only be given to the eligible applicant.
- The company is required to purchase sufficient planting materials from FPDSB and/or its authorized representatives.
- FPDSB holds the first right of refusal to purchase latex and timber from the assigned trees.

Grant Scheme for Agroforestry

- Wednesday, 16 September 2009 12:41 WebMaster
- ***Successful applicant will be given a grant for the development of agro forestry project with the following terms and conditions.***
- The Grant is only for the development of agro forestry.
- The supply of planting materials is from FPDSB or authorized representative of FPDSB and the cost of such supply will be deducted from the grant.
- FPDSB will also appoints the eligible contractor to carry out the development of the project and the cost will be deducted from the grant.
- The individual is responsible to maintain the plantation after all preliminary development has been executed by FPDSB.
- FPDSB holds the first right of refusal to purchase latex and timber from the assigned trees.
- The balance of the grant will be disbursed to the individual progressively for maintenance work.
- Last Updated (Wednesday, 16 September 2009 14:47)
- **QUICK MENU**

Current Status

- Applications for the establishments of 76,000ha involving RM300million loans have been approved.
- 45% have started to embark on planting
- Rubber is popular species in Peninsular Malaysia and Sabah while mix of other 7 species are popular in Sarawak

(ii) New tax incentives to promote forest plantation

A new tax incentive regime will soon be in place to both planting and harvesting phases.

The new tax incentives are provided under the Income Tax Rules 2009 (Deduction for investment in an approved forest plantation project) and the Income Tax Order 2009 (Exemption) (No. 10), which are effective until the end of 2011.

The Tax Exemption Order will allow plantation companies to offset the costs during the planting period against the income from the harvest. The costs can be fully deducted from the aggregate income during the first 10 years of a new forest plantation project, and 5 years for an expanded forest plantation project.

According to the Sarawak Timber Association (STA), investments into any approved forest plantation project of a subsidiary by a holding company may now be deducted at the beginning of the planting period for the purpose of determining the adjusted income of the holding company, resulting in lower income tax for the holding company.

In addition, forest plantation companies are allowed to claim a reinvestment allowance for approved plantation projects. The allowance will be credited through the Exempt Income Accounts for the purpose of declaring dividends. Dividends received by holding companies will not be subjected to taxation.

Six major timber groups in Sarawak including Rimbunan Hijau Group, Samling Global Ltd, WTK Holdings Bhd, Shin Yang Forestry Sdn Bhd, KTS Forest Plantations Sdn Bhd and Ta Ann Holdings Bhd have welcomed this new tax incentive regime.

These groups have been given approval by the Sarawak state authorities to reforest more than 1 million hectares of logged-over areas. The six groups are also among 41 active forest plantation licence-holders in Sarawak.

With the targeted 1 million hectares of forest plantations to be developed, Sarawak could double its supply of raw materials for its timber processing industry.

- As of 2009, up to 255,000 hectares of forest plantations worth RM2 billion in investments (RM7,843 per hectare), have been developed in Sarawak against the set target of 500,000 hectares. Three main fast-growing commercial tree species favoured in forest plantation projects are acacia (*Acacia hybrid*), kelempayan (*Neolamarckia cadamba*) and binuang (*Octomeles sumatrana*). The average establishment cost of all these three species is about RM8,200 per hectare.

The Federal Government grants soft loans to fund forest plantation projects based on the forest plantation area. Applications for such a loan are restricted to 5,000 hectares per application. Earlier, the Ministry of Plantation Industries and Commodities had estimated that some RM1.1 billion was needed to develop 150,000 hectares of forest plantations (RM7,333 per hectare) nationwide from 2006 to 2013.

- As reported in a Local Newspaper in Sarawak from a speech from the Ministry of Plantation and Industrial Commodities (Oct 22 2010)